Office of Chief Counsel
Internal Revenue Service

memorandum

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HEDowns

date: MAY 2 4 2002

to: Technical Support Section, SB/SE, Area 10

from: Associate Area Counsel (SB/SE)

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subject: **Deduction of Political Contributions by Lobbyists under IRC 162**

This is in response to your request dated May 1, 2002.

DISCLOSURE STATEMENT

This advice constitutes return information subject to IRC § 6103, and may contain confidential information subject to attorney-client and deliberative process privileges, and, if prepared in contemplation of litigation, subject to the attorney work product privilege. The recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure.

This advice is not binding on the IRS and is not a final case determination. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

ISSUE

In response to a question for the State of Oklahoma Tax Commission, you determined that registered lobbyists in the trade or business of lobbying may deduct political contributions as business expenses under IRC § 162. You requested our concurrence before communicating this conclusion to the State tax authority.

CONCLUSION

After review of the statutory language and legislative history, we conclude that political contributions are not deductible by professional lobbyist as ordinary and necessary business expenses under IRC § 162.

DISCUSSION

Prior to the end of taxable year 1993, IRC § 162(e)(1)(A) and (B) provided, generally, for deduction of ordinary and necessary expenses paid or incurred in carrying on a trade or business, in direct connection with appearances before, submission of statements to, or sending communications to United States legislators and legislative bodies, or in direct connection to communication of information between a taxpayer and an organization to which the taxpayer belonged with respect to legislation or proposed legislation of direct interest to the taxpayer and the organization. Former IRC § 162(e)(2)(A) and (B) provided the limitation that the provisions of § 162(e)(1) were not to be construed to provide for deduction of any amount paid or incurred by way of contribution, gift or otherwise, for participation in or intervention in any political campaign on behalf of any candidate for public office, or in connection with any attempt to influence the general public with respect to legislative matters, election or referendums.

As of December 31, 1993, IRC § 162 was amended to read, in pertinent part, as follows:

> (e) Denial of deduction for certain lobbying and political expenditures.
> (1) In general. No deduction shall be allowed under subsection (a) for any amount paid or incurred in connection with -
> (A) influencing legislation,
> (B) participation in, or intervention in, any political campaign on behalf of (or in opposition to) any candidate for public office,
> (C) any attempt to influence the general republic, or segments thereof, with respect to elections, legislative matters, or referendums, or
> (D) any direct communication with a covered executive branch official in an attempt to influence the official actions or positions of such official.

Current § 162(e)(5)provides:

> (5) Other Special Rules.
> (A) Exception for certain taxpayers. In the case of any taxpayer engaged in the trade or

> business of conducting activities described in paragraph (1), paragraph (1) shall not apply to expenditures of the taxpayer in conducting such activities directly on behalf of another person (but shall apply to payments by such other person to the taxpayer for conducting such activities).

The legislative history of the amendment of § 162(e) indicates that the reason for the change was to more narrowly limit the business deduction for lobbying expenses, generally. The legislative history also reflects that the then present-law disallowance of business deductions "for expenses of grass roots lobbying and participation in political campaigns" was to remain in effect under the new law. H. R. Rep. No. 103-111, 103d Cong., 1st Sess. (1993).

The language of current § 162(e)(5)(A) is complex. However, a careful reading, in our opinion, indicates that it was intended only to allow professional lobbyist who are engaged in the trade or business of lobbying to deduct their ordinary and necessary expenses of conducting such lobbying activities on behalf of their clients. Ordinary and necessary expenses would include such items as office expense, telephone, postage, travel and entertainment, and other commonly deductible business expenses, subject to the same limitation as apply to such expenses in the context of other business.

Please note, the exception of 162(e)(5)(A) applies only to a lobbyist's expenditures in conducting lobbying activities "directly on behalf of another person...." Making political contributions could not be, in our opinion, an expense incurred on behalf of a specific client in representing clients to legislators or before legislative bodies. Although we did not research campaign finance laws, we suspect it would be inappropriate for lobbyists to make political contributions on behalf of their clients. It is hard to imagine how one would evaluate the ordinary, necessary and reasonable nature of contributions made by a lobbyist, not for a client, but for the general advancement or protection of their business as a lobbyist, if such deductions were allowable.

Admittedly, this is not a settled issue, as no Court has addressed the application of § 162(e) to political contributions or campaign contributions made by professional lobbyist. It is well settled, however, that deductions are strictly a matter of legislative grace, and taxpayers are required to prove entitlement under specific statutory provisions. INDOPCO, Inc.

v. Commissioner, 503 U.S. 79, 84 (1992); New Colonial Ice Co. v. Helvering, 292 U.S. 435, 440 (1934). It is appropriate to read, interpret and apply deduction allowances narrowly. While we would concede that § 162(e)(5)(A) provides for the deduction, by lobbyist in the trade of business of lobbying, of ordinary and necessary business expenses incurred in conducting such business, we would argue that political contributions are not ordinary and necessary business expenses directly related to conducting lobbying activities on behalf of clients.

This argument on behalf of the government, and the taxpayers contrary argument that political contributions are deductible by lobbyists under § 162(e)(5)(A), were raised and briefed in the case of Walker v. Commissioner, T.C. Memo. 1997-76, but the Court declined to address the issue, finding simply that, under the provisions of the older law, which applied to the years at issue in the case, political contributions were clearly not deductible. Contrary to some summaries of Walker that one may read, the Court did not determine that political contributions would be deductible under the new law. The Court simply stated: "We need not address petitioners' argument regarding the current section 162(e)(5)(A), since Congress expressly provided that the section was to be effective only for amounts paid of incurred after December 31, 1993."

To date, no other Court has addressed this issue. The regulations have not been amended to reflect changes to § 162(e), and no specific guidance on the issue has been issued by the IRS or Office of Chief Counsel. Until there is some specific direction regarding allowance of deductions for political contributions for lobbyists, we would advise against issuing any public or general statement that lobbyists' political contributions are deductible.

If you have any questions regarding this memorandum, please call Senior Attorney Elizabeth Downs at 297-4820. This memorandum closes our file.

MICHAEL J. O'BRIEN
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By: /s/ ELIZABETH DOWNS
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